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THE ECONOMY IN BRIEF

DEPARTMENT OF FINANCE DECEMBER 2000

KEY MESSAGES

- In the third quarter of 2000, real gross domestic product (GDP) again increased robustly, rising 4.8%. This was the fifth consecutive quarter of growth above 4.5% and it brought output to 5.0% above its level a year earlier.
- Domestic demand boosted Canadian production. Real final domestic demand (spending by consumers, business and government on goods, services, housing, plant and equipment) increased 5.9%, a similar pace to that in the second quarter. Inventory accumulation was greater than in the second quarter, but foreign demand declined modestly with real exports off 0.5%, partly reflecting the slowdown in the United States. Meanwhile, real import growth weakened to 5.9% from 11.8% in the second quarter, implying that production outside Canada satisfied a smaller part of the increased domestic demand than in the previous quarter.
- The nominal trade surplus fell as the real trade surplus declined to 60% of its second-quarter level. The drop in the nominal surplus, however, was moderated by a sharp gain in the terms of trade (export prices rose while import prices fell). The current account, at $13.5 billion and 1.3% of nominal GDP, registered a third consecutive large surplus.
- Net job creation has been impressive. Employment in November 2000 was more than 715,000 above the level at the end of 1998. The unemployment rate in November was 6.9%, the same as in October.

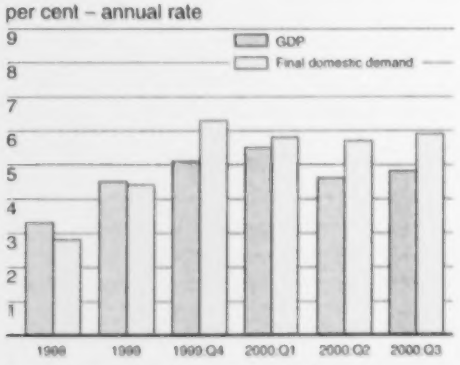
SUMMARY[1]

In the third quarter of 2000, the Canadian economy continued its solid growth, the 21st consecutive quarterly gain and the longest uninterrupted string of advances since the mid-1960s. Increased domestic demand provided the boost to Canadian production, as foreign demand eased back (Chart 1).

Consumer spending strong and durable

Real consumer expenditure increased at a stronger pace than in the second quarter, rising 5.5%. While gains were widespread, spending on durables was especially strong, surging

Chart 1
Growth in real GDP and real final domestic demand



Note: Final domestic demand is spending by Canadians on goods, services, housing, plant and equipment.

[1] Unless otherwise noted, data and per cent changes are quoted at annual rates. The cut-off date for data is noon, December 1, 2000.

Main economic indicators
(per cent change at annual rates unless otherwise indicated)

	1998	1999	2000:Q1	2000:Q2	2000:Q3		Most recent
Real gross domestic product	3.3	4.5	5.5	4.6	4.8		–
GDP excluding inventories	3.9	4.7	6.0	4.9	3.0		–
Final domestic demand	2.8	4.4	5.8	5.7	5.9		–
Government expenditure	1.6	2.8	5.8	4.7	4.0		–
Consumer expenditure	2.9	3.5	4.0	3.6	5.5		–
Residential investment	-2.0	6.6	2.3	-9.4	6.0		–
Business fixed investment	6.1	10.5	15.1	22.9	10.5		–
Non-residential construction	1.7	2.0	10.3	2.8	-0.5		–
Machinery and equipment	9.0	15.6	17.[illegible]	34.0	16.0		–
Business inventory change[1]	-0.5	-0.2	-0.[illegible]	-0.3	1.7		–
Trade balance[1]	1.1	0.4	0.[illegible]	-0.8	-2.6		–
Exports	8.9	10.0	15.5	9.3	-0.5		–
Imports	6.1	9.4	15.4	11.8	5.9		–
Current account balance							
(nominal $ billion)	-16.3	-3.4	18.3	14.4	13.5		–
(percentage of GDP)	-1.8	-0.4	1.8	1.4	1.3		–
Real personal disposable income	2.8	2.7	8.3	3.0	-1.2		–
Profits before taxes	-5.6	23.7	32.6	8.9	4.2		–
Costs and prices (%, y/y)							
GDP price deflator	-0.6	1.6	3.7	3.6	3.4		–
Consumer price index	0.9	1.7	2.7	2.4	2.7	2.8	Oct-2000
CPI – excluding food and energy	1.3	1.5	1.5	1.4	1.5	1.5	Oct-2000
Unit labour costs	1.4	0.5	1.7	2.3	2.2		
Wage settlements (total)	1.7	2.2	2.4	2.5	2.3	2.7	Sep-2000
Labour market							
Unemployment rate (%)	8.3	7.6	6.8	6.7	6.9	6.9	Nov-2000
Employment growth	2.7	2.8	3.8	1.6	0.7	4.8	Nov-2000
Financial markets (average)							
Exchange rates (cents U.S.)	67.48	67.32	68.80	67.56	67.47	64.86	30-Nov-2000
Prime interest rate (%)	6.60	6.44	6.75	7.33	7.50	7.50	30-Nov-2000

[1] Annualized change expressed as a percentage of GDP in the previous period.
Sources: Statistics Canada, the Bank of Canada and Human Resources Development Canada.

16.3%. Growth in personal spending on automotive products was particularly robust, as manufacturers offered incentives to boost sales of motor vehicles.

The 3.2% gain in personal income was half that in the second quarter. Labour income growth slowed sharply as employment growth moderated and the federal pay equity disbursements were much smaller than in the second quarter. The personal savings rate fell to 2.3% from 3.9% in the second quarter.

Productive capacity continues to grow

Businesses further enhanced their productive capacity in the third quarter, as investment in plant and equipment rose 10.5%. However, growth was more moderate than the 22.9% surge in the second quarter. Following a 34% jump in the second quarter, machinery and equipment investment rose 16%, led by a 50% gain in telecommunications and computers and other office equipment. Non-residential construction, however, declined modestly, with drops in both building and engineering projects.

Residential investment increased 6% in the third quarter following a sharp decline of 9.4% in the second. New construction activity rose along with housing starts, rebounding from a second-quarter strike in the Toronto area. Growth rates for renovations and transfer costs were similar to that for new construction.

Stronger inventory accumulation

Inventory accumulation in the third quarter significantly surpassed that in the second, adding to GDP growth. Business inventories increased $11.6 billion after rising $7.7 billion in the earlier quarter. The greater accumulation largely reflected buildups in motor vehicles produced for the American market and information and communications technology products. But with sales growth just exceeding that of inventories, the inventory-to-sales ratio inched down to a new record low.

Domestic demand boosts Canadian production while foreign demand sags

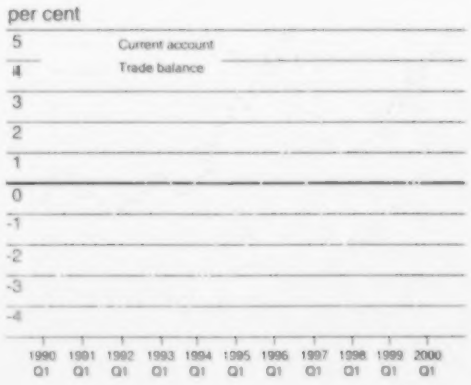
Increased domestic demand raised real imports by 5.9%, half the pace of the second quarter. Imports thus accounted for a smaller part of increased domestic demand than in the previous quarter. This slowdown partly stemmed from the reduced growth in investment in machinery and equipment, an import-intensive category of domestic demand.

Reduced foreign demand for Canadian products, partly reflecting the sharp growth slowdown in the United States to its weakest pace in four years and to only half that in Canada, lowered real exports 0.5% in the third quarter. While there was a sharp growth slowdown in exports of machinery and equipment, especially those of the "new economy," the drop was largely due to reduced exports of automotive and energy products. Energy exports responded negatively to higher world prices. Weaker automotive exports is consistent with the modest growth in U.S. motor vehicle sales in the third quarter after falling sales in the second quarter. With real imports rising and real exports falling modestly, the real trade balance was about 60% of that in the previous quarter.

Another large current account surplus

While the real trade balance was sharply lower, export prices rose and import prices fell. This produced an improvement in the terms of trade of over 5%, leaving the nominal trade surplus at a high level and only about $0.5 billion lower than in the second quarter. However, a deterioration in the transfers balance more than offset an improvement of over $1 billion in the investment income (including retained earnings) deficit. Thus the current account surplus dropped to $13.5 billion, or 1.3% of nominal GDP, from $14.4 billion in the second quarter (Chart 2). While below the record of $18.3 billion (1.8% of nominal GDP) in the first quarter, the continuing large current account surplus represents a substantial improvement from deficits of 1.8% of nominal GDP in 1998 and 0.4% in 1999.

Chart 2
Current account as a percentage of nominal GDP



Inflation subdued as productivity up again

Underlying price and cost pressures remain subdued. The implicit and chain price indices for GDP advanced in the third quarter to levels 3.4% and 4.2% higher than a year earlier. The size of these increases partly reflected the temporary impacts of higher energy prices. And while consumer price inflation remained just below 3.0% in October on a year-over-year basis, the increased pace relative to recent years is again largely due to higher energy prices. Underlying CPI inflation, which excludes food and energy, was only 1.5% in that month on a year-over-year basis.

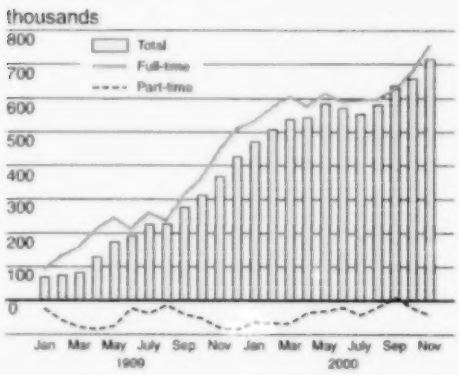
Labour productivity registered another strong gain, one that was larger than those in the first and second quarters: output per hour worked was up nearly 5% in the third quarter while output per employed person rose over 4%. Productivity growth plus smaller pay equity disbursements caused year-over-year unit labour cost growth to slow to 2.2%.

Pre-tax corporate profits rose 4.2%, the eighth consecutive increase, to a level 17.5% above that of a year earlier. Gains were notable for the oil and gas extraction industry, given higher energy prices, and for electronics and computer manufacturers, given strong demand for their products.

Unemployment remains low

Third-quarter employment growth eased further to 0.7% from 1.6% in the second. But with some 58,000 net new jobs created in November, employment has risen by nearly 290,000 so far in 2000 (Chart 3). The total increase since the end of 1998 stands at over 715,000 jobs. Full-time jobs have exceeded the total net gain, as part-time employment fell over that period. The unemployment rate in November 2000 was 6.9%, the same as in October.

Chart 3
Cumulative employment growth since December 1998



The Canadian dollar loses some ground

After trading near 68 cents U.S. in late August, the dollar closed at 64.86 cents U.S. on November 30.

The U.S. Federal Reserve and the Bank of Canada have continued to monitor the impacts of earlier monetary tightening aimed at staving off inflationary pressures. While administered interest rates have remained steady since the end of May, short-term market rates in the United States increased until late August but have shown little trend since. Meanwhile, long rates have continued to trend downward. In Canada, short-term interest rates have risen somewhat since the end of August while long rates have declined, although not as much as in the United States. As a result, short rates in Canada have remained well below those in the United States while long-term rates in the two countries are at similar levels. The differential between Canadian and U.S. 3-month Treasury bill yields generally has remained over 60 basis points since the end of August.

The main source of data used in this publication is Statistics Canada. Subscription inquiries should be directed to the Distribution Centre at (613) 995-2855. For other inquiries about this publication, contact Mostafa Askari at (613) 992-3055.
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